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1. Cross-References within the Internal Revenue Code of 1954 as of January 1, 1961

2. Suggested Methods of Liberalizing Depreciation

3. Refunds and Credits of Internal Revenue Taxes for the Fiscal Year Ended June 30, 1959

4. Comparison of Existing Law with President's Proposals on Taxation of Income from Foreign Subsidiaries

5. Digest of Testimony Presented and Statements Submitted to the Committee on Ways and Means with Respect to the President's Tax Recommendations

6. Tax Effects of Conducting Foreign Business Through Foreign Corporations

7. Estimates of Federal Receipts for the Fiscal Year 1962

8. History of Exemption of Dividend Income Under the Individual Income Tax 1913-1961

9. General Explanation of Committee Discussion Draft of Revenue Bill of 1961

10. Federal Excise-Tax Data

11. Report on the Renegotiation Act of 1951 (H. Doc. 322)

12. Cross-References within the Internal Revenue Code of 1954 as of Jan. 1, 1962

13. Summary of the Revenue Bill of 1962 As It Passed the House (H.R. 10650)

14. Digest of Testimony Presented and Statements Submitted to the Committee on Finance with Respect to H. R. 10650

15. (Conf.) Supplemental Digest of Testimony Presented and Statements Submitted to the Committee on Finance with Respect to Foreign Income Tax Sections of H. R. 10650

16. Analysis of Section 19 of H. R. 10650 Withholding on Dividends and Interest

17. (Conf.) Suggestions for Amendments to H. R. 10650

18. Summary of Revenue Bill of 1962 As Reported by the Senate Committee on Finance (H. R. 10650)

19. Summary of Senate Amendments to H. R. 10650

20. Summary of the Provisions of the Self-Employed Individuals Tax Retirement Act of 1962 (H. R. 10)

HISTORY OF EXEMPTION OF DIVIDEND INCOME UNDER THE INDIVIDUAL INCOME TAX 1913–1961

PREPARED BY THE

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JULY 25, 1961

U.S. GOVERNMENT PRINTING OFFICE
72850 WASHINGTON : 1961 JCS 6–61

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EXEMPTION OF DIVIDEND INCOME UNDER THE INDIVIDUAL INCOME TAX, 1913–61

The concept in the early days of the Federal income tax was that corporate earnings would be subject: (*a*) at the corporate level to the basic or "normal" tax rate common to the corporate income tax and the individual income tax; and (*b*) at the shareholder level to only the graduated surtax rates of the individual income tax. Thus, from 1913 to the end of 1935, dividends received by individuals were not subject to the normal tax on individual income. However, it was only from 1913 to 1917 that the corporate income tax was set at the same rate as the individual normal income tax. During this period, generally speaking, the effect of the dividend exemption or credit was to render dividend income subject to only the tax rates of the individual normal tax and surtax. But from 1917 on, the corporate rate exceeded the individual normal income tax rate and to that extent what is considered by many to be double taxation of dividend income began.

Under the 1913 act, corporate net income was subject to a 1-percent tax rate while individual net income was subject to a normal tax rate of 1 percent and a surtax at rates graduated from 1 to 6 percent. Dividends received by stockholders were exempt from normal tax. Thus, corporate earnings were subject to a 1-percent tax at the corporate level but exempt from the 1-percent normal tax on individual income at the stockholders' level and subject to the individual income surtax at rates graduated from 1 to 6 percent at the stockholders' level.

Under the Revenue Act of 1916, the corporate net income tax rate and the normal individual income tax rate were increased to 2 percent with dividends continuing to be exempt from the individual normal tax.

Under the Revenue Act of October 3, 1917, the corporate rate was increased to 6 percent while the individual normal tax rate, against which dividend income was credited, was increased from 2 percent on all normal tax net income to 2 percent on the first $2,000 of such income and 4 percent on such income over $2,000. In calendar year 1918, the corporate rate of 12 percent coincided with the rate applicable to individual normal tax net income over $4,000 but exceeded the 6-percent rate applicable to the first $4,000 of such income. Thus, while corporate dividends continued to be exempt during this period from the individual normal income tax, the tax rate to which the dividend credit applied was no longer fully equivalent to the rate levied on corporate earnings at the corporate level.

From 1919 on, the corporate rate continued to exceed the individual normal rate with the gap gradually widening until 1936 when the connection between the two taxes was completely severed by the elimination of the dividend exemption. (It is interesting to note that in 1935, the last year in which this early dividend-received credit was

effective, the individual normal tax rate to which the credit applied was 4 percent, the same as the current rate of the dividend-received credit against tax.)

The revenue bill of 1936, as passed by the House, proposed the elimination of the normal tax on corporations and the substitution of a tax on corporate net income whose rates would vary with the size of the corporate net income and the percentage of the net income that would be undistributed. Under the bill, a corporation which distributed its entire income would pay no tax. In order that distributed corporate earnings would be fully taxed in the hands of shareholders, the bill would repeal the then existing dividend credit for purposes of the individual normal tax.

As finally enacted, the Revenue Act of 1936 retained the normal tax on corporations with slightly altered rates and imposed a graduated surtax on undistributed net income, but—because of the need for revenue—failed to restore the dividend credit for purposes of the individual net income tax.

Under the 1954 code, the tax on dividend income was reduced in two related provisions. Under one (sec. 116) an individual may exclude from his gross income up to $50 of dividend income received from a domestic corporation. A husband and wife filing a joint return have two exclusions where each is a dividend recipient. The other provision (sec. 34) makes available a dividend-received credit against tax equal to 4 percent of dividend income above the $50 exclusion.